United States Court of Appeals

for the Second Circuit

APPELLANT'S BRIEF

74-1633

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In The
UNITED STATES COURT OF APPEALS
For The Second Circuit

To be
argued by
Thomas A. Butler

IN RE

PENN CENTRAL COMMERCIAL PAPER
LITIGATION

ALEX SHULMAN, Plaintiff,

-against-

GOLDMAN, SACHS & CO., et al. Defendants.

SEATTLE-FIRST NATIONAL BANK, Applicant.

BRIEF FOR APPELLANT

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Docket No. 74-1633

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BRIEF OF APPELLANT

STATEMENT OF ISSUES

1. Did the district court err in denying appellant's motion to intervene as of right pursuant to F.R.C.P. 24(a)(2)?

2. Did the district court err in denying appellant's motion for permissive intervention pursuant to F.R.C.P. 24(a)(2)?

3. Did the district court err in denying appellant's motion for consolidation pursuant to F.R.C.P. 42(a)?

STATEMENT OF THE CASE

This is an appeal from the order of Chief Judge David N. Edelstein of the United States District Court for the Southern District of New York dated April 4, 1974, denying the motion of appellant Seattle-First National Bank ("Seattle") (i) for intervention as of right or with the court's permission pursuant to F.R.C.P. Rules 24(a)(2) and 24(b)(2) in Alex Shulman v. Goldman, Sachs & Co. et al., 71 Civ. 1996 (DNE) ("Shulman I") or (ii) to consolidate Alex Shulman v. Seattle-First National Bank, (W.D. Washington Civ. No. 9760) 72 Civ. 616 (DNE) ("Shulman II") with Shulman I pursuant to F.R.C.P. rule 42(a). Chief Judge Edelstein's opinion was reported at 62 F.R.D. 341.

FACTS

On or about May 5, 1971, Alex Shulman commenced Shulman I in the Southern District of New York to recover the $300,000 face value of a commercial paper note of the Penn Central Transportation Company ("Penn Central") purchased from Goldman, Sachs & Company ("Goldman, Sachs"). (R. 10a) Shulman alleges

that Seattle, acting as his agent, purchased the note from Goldman, Sachs. (R. 44a-45a) Prior to the maturity date of the note Penn Central filed for reorganization and the note was never paid. (R. 9a-10a)

On or about June 16, 1971, Shulman commenced Shulman II in the Western District of Washington to recover the same $300,000 from Seattle. (R.10a-11a) Thereafter, Seattle in Shulman II impleaded Goldman, Sachs. (R.11a) Both Shulman I and II were consolidated for purposes of coordinated pretrial proceedings in MDL-56A (DNE). (R. 12a-13a)

Shulman's claim against Goldman, Sachs in Shulman I is that in connection with its sale of the note to Shulman, Goldman, Sachs failed to disclose certain material facts and misrepresented other facts regarding the financial condition of Penn Central in violation of the federal and state securities laws as well as other laws. In Shulman II, Shulman alleges the same misrepresentations and omissions as it alleges in Shulman I but asserts that they were committed by Seattle acting in concert with Goldman, Sachs. (R. 62a-65a) In its third party claim in Shulman II, Seattle alleges that it was the victim of misrepresentations and omissions which are the same as those alleged

in the Shulman I complaint. (R. 74a) Goldman, Sachs, as a defense to the Shulman I complaint and the Shulman II third party complaint, alleges that Shulman and Seattle, respectively, had full knowledge of all material facts relevant to the purchase of the note. (R. 56a and 81a)

By notice of motion dated January 23, 1974, Seattle moved to intervene as of right or with the court's permission in Shulman I. (R. 5a-6a) Seattle's proposed intervention complaint asserts, as in its third party complaint in Shulman II, that it was defrauded by Goldman, Sachs in the sale of the note. The misrepresentations and omissions by Goldman, Sachs are substantially identical to those alleged by Shulman against Goldman, Sachs in Shulman I. Seattle moved, in the alternative, to consolidate Shulman I and II. (R. 5a-6a) Chief Judge Edelstein denied both intervention and consolidation. (R. 83a)

POINT I

THE DISTRICT COURT ERRED IN DENYING SEATTLE'S MOTION TO INTERVENE AS OF RIGHT

Seattle has a right to intervene in Shulman I. Rule 24(a)(2) of the Federal Rules of Civil Procedure provides for intervention as of right

> "...when the applicant claims an interest relating to the property or transaction which is the subject of the action and he is so situated that the disposition of the action may as a practical matter impair or impede his ability to protect that interest, unless the applicant's interest is adequately represented by existing parties."

Seattle's application for intervention as of right satisfies each of the three requirements set forth in Rule 24(a)(2).

A. The district court erred in holding that Seattle had no interest relating to the property or the transaction which is the subject of Shulman I.

The district court adopted an erroneously stringent standard in evaluating whether Seattle had met the "interest" requirement. Even under the district court's standard, however, Seattle has an interest relating to the property and the transaction which is the subject of Shulman I.

(1) The district court applied the wrong standard to determine whether the "interest requirement" has been met.

The interest requirement of Rule 24(a)(2) is the least critical of the three requirements which a party must meet to be entitled to intervene as of right. Smuck v. Hobson, 408 F.2d 175 (D.C. Cir. 1969); Nuesse v. Camp, 385 F.2d 694 (D.C. Cir. 1967). The interest requirement is basically a "practical guide to disposing of lawsuits by involving as many apparently concerned persons as is compatible with efficiency and due process." 385 F.2d at 700. The Court in Smuck, in emphasizing the limited importance of the interest requirement, stated:

> "...the first requirement of Rule 24(a)(2), that of an 'interest' in the transaction, may be a less useful point of departure than the second and third requirements, that the applicant may be impeded in protecting his interest by the action and that his interest is not adequately represented by others.
>
> This does not imply that the need for an 'interest' in the controversy should or can be read out of the rule. But the requirement should be viewed as a prerequisite rather than relied upon as a determinative criterion for intervention. If barriers are needed to limit extension of the right to intervene, the criteria of practical harm to the applicant and the adequacy of represen-

> tation by others are better suited to the task. If those requirements are met, the nature of his 'interest' may play a role in determining the sort of intervention which should be allowed--whether, for example, he should be permitted to contest all issues, and whether he should enjoy all the prerogatives of a party litigant."
> 408 F.2d at 179-180.

The district court, in denying intervention, adopted an erroneously stringent standard for determining whether Seattle satisfied the "interest" requirement. In doing so, it relied on Donaldson v. United States, 400 U.S. 517 (1971). This reliance was misplaced. Donaldson involved a tax enforcement summons proceeding. As Professor Wright has pointed out:

> "Donaldson, like Cascade, hardly can be read without giving thought to its facts. A broad reading of the intervention rule was thought necessary in Cascade in order to protect the public interest in effective competition. A narrow reading of the intervention rule was thought necessary in Donaldson in order to protect the public interest in prompt and effective investigation and enforcement of the revenue laws. The Donaldson case is greatly colored by the fact that this is a special summary proceeding in which the rules are not universally applicable.

> For these reasons, it seems that any attempt to extrapolate from Cascade or from Donaldson, and to deduce from those cases rules applicable to ordinary private litigation, is fraught with great risks. The Court did say in Donaldson that the word 'interest' in Rule 24(a)(2) 'obviously means a significantly protectable interest'. Lower courts cannot ignore this direct interpretation of the rule by the Supreme Court. But 'significantly protectable interest' has not been a term of art in the law and there is sufficient room for disagreement about what it means so that this gloss on the rule is not likely to provide any more guidance than does the bare term 'interest' used in Rule 24 itself." Wright & Miller, Federal Practice and Procedure, Civil § 1908, at 502.

Donaldson, therefore, should not be read to restrict Seattle's right to intervene in Shulman I, an action between private litigants.

The district court, also, applied its erroneously stringent standard in holding that intervention was precluded because Seattle could not maintain an independent action against Goldman, Sachs. An applicant for intervention does not have to assert a claim which states an independent cause of action in order to be entitled to intervention as of right. Trbovich v. United Mine Workers of America, 404 U.S. 528 (1972). D. Shapiro, Some Thoughts on Intervention Before Courts, Agencies and Arbitrators, 81 Harv. L. Rev. 721, 726-729, 735-749 (1968). In his article

which was relied upon by the Court in Trbovich, Professor Shapiro explains:

> "Perhaps it should go without saying, but it must be understood that there is a difference between the question whether one is a proper plaintiff or defendant in an initial action and the question whether one is entitled to intervene. Thus, to decide whether a particular action may be brought by this plaintiff against this defendant may require a determination of whether the controversy is ripe for adjudication, whether the parties before the court are the real parties in interest, and whether the interests asserted are sufficient to mobilize the judicial machinery. When one seeks to intervene in an ongoing lawsuit, these basic questions have presumably been resolved; the disposition of the request, then, should focus on whether the prospective intervener has a sufficient stake in the outcome and enough to contribute to the resolution of the controversy to justify his inclusion. In the federal courts, at least, this distinction in some instances may be of constitutional dimensions. A may not have a dispute with C that could qualify as a case or controversy, but he may have a sufficient interest in B's dispute with C to warrant his participation in the case once it has begun, and the case or controversy limitation should impose no barrier to his admission." Shapiro, supra at 726 (footnotes omitted)

Trbovich involved an application for intervention by a union member in an action brought by the Secretary of Labor pursuant to the Labor-Management Reporting and Disclosure Act ("LMRDA") to set aside a union election. The Secretary opposed intervention on the grounds that LMRDA expressly precluded union

members from maintaining an action to set aside a union election. The Supreme Court held that the union member was entitled to intervene as of right. The Court held that the question of whether a party can intervene and the question of whether a party can initiate an independent action are fundamentally different questions. Even though LMRDA would prohibit union members from maintaining an independent cause of action, the Court determined that the union member could intervene because he had an interest in the proceeding and otherwise satisfied the requirements of Rule 24(a)(2).

The district court erred in deciding whether Seattle had a sufficient interest to intervene as of right because it applied an erroneous standard out of keeping with the intent of Rule 24(a)(2). The failure of the district court to apply the correct standard is sufficient grounds for reversal.

(2) Seattle has satisfied the interest requirement.

Seattle has a significantly protectable interest in the transaction which is the subject of Shulman I even under the standard adopted by the district court. Seattle was significantly involved in the sale of the $300,000 Penn Central Commercial

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paper note by Goldman, Sachs to Alex Shulman. Seattle acted as Shulman's agent in the purchase of the note. In Shulman I, Shulman charges Goldman, Sachs with fraud in the sale of the note. The subject of Shulman II is the identical transaction. In Shulman II, Shulman charges Seattle with the same fraud as alleged against Goldman, Sachs in Shulman I. In Shulman II, Shulman alleges that Seattle acted in concert with Goldman, Sachs. Seattle, in Shulman II, has impleaded Goldman, Sachs for fraud in the sale of the note. The fraud alleged by Seattle against Goldman, Sachs is based on the identical omissions and misrepresentations which form the basis of Shulman's claim against Goldman, Sachs in Shulman I. Seattle's involvement in the sale of the note and the lawsuits resulting from the sale gives it interests which are entitled to protection through intervention. Among the interests are the protection of Seattle's rights in Shulman II and of its reputation.

B. Seattle is so situated that the disposition of Shulman II may as a practical matter impair or impede its ability to protect its interests.

Because Shulman I and II are substantially identical, they present common legal issues. Seattle's ability to protect its interests in Shulman II

as a practical matter may be impaired by the application of principles of stare decisis. The stare decisis effect of Shulman I was held to be insufficient to meet the "impairment" test of Rule 24 (a)(2) because, in the district court's view, the decision of one district court is not binding upon another, but is only persuasive, and hence it "cannot be said with any certainty that the outcome of Shulman I will impair Seattle-First's ability to protect itself in Shulman II." 62 F.R.D. at 347. The court's reasoning and conclusions are erroneous. The effect of stare decisis is, of course, never binding or certain. It is, at most, only persuasive. However, there is no requirement under Rule 24 (a)(2) that a party will be bound by the action in which it desires to intervene, or that there be a certainty that it will be damaged by the decision of the action in which it desires to intervene. To the contrary, the 1966 amendments to Rule 24 (a)(2) were designed to eliminate such requirements. Nuesse v. Camp, 385 F. 2d at 701. The rule merely requires that the "disposition of the action may as a practical matter impair or impede his ability to protect his interest." (emphasis added.)

In an appropriate case stare decisis may by itself supply this possibility of impairment. Nuesse v. Camp, supra; Martin v. Travelers Indemnity Company, 450 F.2d 542, 554 (5th Cir. 1971); Atlantis Development Corporation v. United States, 379 F.2d 818 (5th Cir. 1967).

This is just such a case. The danger that the determination of the issues of law in Shulman I will be adopted in Shulman II is particularly great because Shulman I and II both involve the identical sale of the same commercial paper note from Goldman, Sachs to Shulman through Seattle as Shulman's agent and liability in both cases depends largely on answers to the same questions. The Fifth Circuit in Atlantis Development Corporation pointed out:

> "...We are dealing here with a conjunction of a claim to and interest in the very property and action. When those coincide, the Court before whom the potential parties in the second suit must come must itself take the intellectually straight forward, realistic view that the first decision will in all likelihood be the second and the third and the last one. Even the possibility that the decision might be overturned by en banc ruling or reversal on certiorari does not overcome its practical effect, not just as an obstacle, but as the forerunner of the actual outcome. In the face of that, it is 'as a practical matter' a certainty

> an absent party seeking a right to enter the fray to advance his interest against all or some of the parties as to matters upon which he is for all practical purposes shortly to be foreclosed knows the disposition in his absence will 'impair or impede his ability to protect that interest.* * *' F.R. Civ. P. 24 (a)(2)." 379 F. 2d at 829.

The significance and authority of any district or circuit court decision in Shulman I will be increased because the legal issues involved relate to the status of commercial paper under the securities laws, an area of great uncertainty in the law in which there are few authoritative precedents. See, Nuesse v. Camp, 385 F. 2d at 702.

The authoritative nature of any decision of law in Shulman I, also, will be enhanced by the status of the court rendering it. Shulman I will be tried in the United States District Court for the Southern District of New York, a district court whose expertise and experience in securities law is unparallelled among district courts. Additionally, if Shulman I is appealed, it will be decided by a panel of the nation's foremost appellate court in the securities area. Moreover, if the Shulman II court disagrees with the decisions of law adopted in Shulman I, the administration of justice

would be impaired by the conflicting decisions. Nuesse v. Camp, 385 F. 2d at 702.

While stare decisis, in this case, by itself satisfies the "impairment" requirement of Rule 24 (a)(2), Seattle's reputation may be impaired in Shulman I. Shulman I will involve necessarily the question of whether Seattle committed fraud. Allegations of fraud whether or not proved will be damaging to Seattle's reputation. This damage can never be cured by a decision favorable to Seattle in Shulman II. Seattle is entitled to intervene so that it may properly present all the facts to the court and public at large in order to protect its reputation as an honest and dependable banking institution. Dodd v. Reese, 216 Ind. 449, 24 N.E.2d 995 (Supreme Court Indiana 1940).

C. Seattle's interest is inadequately represented in Shulman I.

The test whether the interest of an applicant for intervention is adequately represented is set out in Trbovich v. Mine Workers, 404 U.S. supra at 538, n 10:

POINT II

THE DISTRICT COURT ABUSED ITS DISCRETION IN NOT ALLOWING SEATTLE TO INTERVENE PURSUANT TO F.R.C.P. 24(b)(2)

Rule 24(b)(2) of the Federal Rules of Civil Procedure provides that an applicant may be permitted to intervene

> "when an applicant's claim or defense and the main action have a question of law or fact in common... In exercising its discretion the court shall consider whether the intervention will unduly delay or prejudice the adjudication of the rights of the original parties."

A. Shulman I and II have common issues of fact and law.

There is no dispute that there are common issues of law and fact. Shulman I and II are substantially identical. In his memorandum in opposition to Seattle's motion to intervene below, Shulman concedes "although the two actions are by no means identical we do not disagree with Seattle-First's claim that the two actions involve many common issues of law and fact."

B. Seattle's intervention in Shulman I will not unduly delay or prejudice the adjudication of the rights of Shulman or Goldman, Sachs.

The court denied Seattle's motion for permissive intervention on the ground that Seattle had demonstrated no benefit which would outweigh the delay incident

to adding another party. Again, the court applied an erroneously restrictive standard. After it has determined that a common question of law or fact exists, a court must determine whether intervention will unduly delay or prejudice the adjudication of the rights of the original parties. The district court made no finding that Seattle's intervention would unduly delay Shulman I or prejudice the rights of Shulman or Goldman, Sachs. Instead, it pointed only to the incidental delay inherent in all intervention. The district court imposed on Seattle the burden of affirmatively demonstrating that there was some benefit which outweighed the incidental delay inherent in all intervention. The failure of the district court to find undue delay and its imposition of a burden on Seattle contrary to Rule 24(b)(2) warrants reversal.

Even under the court's standard the advantages of intervention outweigh any disadvantages. Seattle's intervention in Shulman I would not delay the trial of Shulman I because Seattle, in its status as a defendant and third party plaintiff in Shulman II, has been involved in all pretrial and discovery

proceedings to date. All discovery necessary to Shulman's and Seattle's claims against Goldman, Sachs and to Goldman, Sachs' defenses to both claims has been completed. Seattle has retained New York counsel who are prepared to go to trial at the earliest date convenient to the parties and the Court.

The addition of Seattle as an intervenor in Shulman I will not result in any prejudice or greater costs to the parties. Goldman, Sachs would not be prejudiced because it already is defending against the same factual and legal allegations raised by Seattle because they are also raised by Shulman. Shulman would not be prejudiced because no claim is being asserted against him and Seattle would be cooperating with Shulman in prosecuting his claim against Goldman, Sachs.

Seattle's intervention in Shulman I would eliminate any possibility of prejudice to Seattle. It would eliminate the possible prejudice to Seattle's claim against Goldman, Sachs in Shulman II resulting from stare decisis and afford Seattle the opportunity to prevent damage to its reputation. Intervention

would make Seattle a party to Shulman I. As a result, Seattle would be estopped from relitigating, in its claim over against Goldman Sachs in Shulman II, all issues of fact and law which are decided against it in Shulman I. This would reduce substantially the scope of Shulman II.

Intervention would permit Seattle to litigate its claims in the forum which can resolve Seattle's claim with maximum judicial economy and efficiency. Proof of Seattle's claim in Shulman II requires the testimony of the same witnesses, most of whom are in New York, who will testify in Shulman I. Because Seattle's intervention in Shulman I may eliminate its claim against Goldman, Sachs in Shulman II, intervention would make it unnecessary for these same witnesses to testify in Shulman II.

The district court stated that permissive intervention was inappropriate because "this court is in no position to grant any relief to Seattle in the absence of a determination in Shulman II which will cause it to incur damages as a result of the transaction which underlies both cases." Again, the court has erroneously taken the position that an applicant is required to state an independent cause

of action for damages in order to intervene. (See pp. 8-10 above) If there are any practical problems arising out of the relief sought, the solution is not to deny intervention. The solution is to impose upon the parties conditions necessary to the efficient conduct of the proceedings. Ionian Shipping Company v. British Law Insurance Co., 426 F. 2d 186, 191-192 (2nd Cir. 1970).

POINT III

THE COURT ERRED IN HOLDING IT HAD NO POWER TO CONSOLIDATE SHULMAN I AND II

Rule 42 (a) of the Federal Rules of Civil Procedure provides:

> "When actions involving a common question of law or fact are pending before the court, it may order a joint hearing or trial of any or all the matters in issue in the actions; it may order all the actions consolidated; and it may make such orders concerning proceedings therein as may tend to avoid unnecessary costs or delay."

It is undisputed that Shulman I and II have numerous common questions of law and fact. Both actions are ready for trial and there is little doubt that a consolidated action would be speedier, less expensive and more just. The district court did not deny Seattle's motion because it disagreed with this. Rather it concluded that Shulman II was not an action "pending before the court" as required by Rule 42 (a). The district court held that it did not have the power to consolidate Shulman I and II unless Shulman II were first transferred to the district court pursuant to 28 USC 1404(a). It further held that such a transfer was impossible. These conclusions are erroneous.

The district court recognized "Shulman II is pending before this Court pursuant to 28 U.S.C. §1407" for pretrial proceedings. 62 F.R.D. 344 (R. 87a) In Humphreys v. Tann, 487 F. 2d 666, 667 (6th Cir., 1973), cert. denied ____ U.S. _____, the Court held that a narrow construction should not be placed on the term "pretrial proceedings." Humphreys points out that while "discovery by deposition, interrogatories and requests for admissions is a part of pretrial proceedings in the typical case, such proceedings are not limited to those activities. Various motions may properly be made as part of pretrial proceedings..." 487 F. 2d at 667-8. For instance, in Pfizer v. Lord, 447 F. 2d 122 (2nd Cir. 1971), this Court held that a transferee court had inherent power to resolve a motion for change of venue.

Seattle's motion for consolidation is a pretrial motion. A motion for consolidation, just as a motion for change of venue, is within the inherent power of a transferee court to determine. Because Shulman II is before the district court, there is no need for a §1404(a) transfer. The inherent power of a

transferee court to decide a motion for consolidation or change of venue is necessary to effectuate the purpose of the multi-district legislation to promote the just and efficient resolution of related actions with a maximum of judicial economy.

CONCLUSION

The substantially identical claims and defenses of Shulman, Seattle and Goldman, Sachs, as well as the common transaction underlying Shulman I and II, make intervention or consolidation appropriate. No sufficient reason for denying intervention was given by the district court. The reason given for denying consolidation was based upon an erroneous view of the district court's power. The district court's denial of Seattle's motion promotes just the sort of "fragmented approach that the revitalized federal rules seek to avoid". Nuesse v. Camp, 385 F.2d at 702.

WHEREFORE, FOR THE REASONS STATED ABOVE, APPELLANT RESPECTFULLY REQUESTS THAT THIS COURT REVERSE THE DECISION OF THE DISTRICT COURT AND REMAND THIS CASE TO THAT COURT WITH INSTRUCTIONS TO ORDER THAT SHULMAN I AND II BE CONSOLIDATED OR THAT APPELLANT BE PERMITTED TO INTERVENE IN SHULMAN I.

Respectfully submitted,

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Raymond Fitzgerald,
Of Counsel

STATE OF NEW YORK
ss.:
COUNTY OF NEW YORK

LON BANNETT being duly sworn, deposes and says, that deponent is not a party to the action, is over 18 years of age and resides at 200 Park Avenue, New York, New York 10017. That on the 27th day of December, 1974, deponent served two copies of the within Brief upon each of the attorneys listed on the cover of the Appendix by depositing true copies of same enclosed in posted properly addressed wrappers, in an official depository under the exclusive care and custody of the United States post office department within the State of New York.

Lon Bannett
LON BANNETT

Sworn to before me this
27th day of December, 1974

Raymond L. Fitzgerald

RAYMOND L. FITZGERALD
Notary Public, State of New York
No. 31-4503159
Qualified in New York County
Commission Expires March 30, 1975